Experian Collections Strategies

Guide Two: Extending the depth of collections capabilities

Experian™
Decision Analytics

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1. Executive Summary

There are numerous approaches to arrears management in the financial sector and an increasing requirement for lenders to further refine their decision strategies, segmentation and collections activities.

As the second in our series of expert guides to quick wins in collections, we assess how some organisations are choosing to drill down deeper and use the full power of their decisioning or collections systems, to implement more proactive and individually tailored collections strategies.

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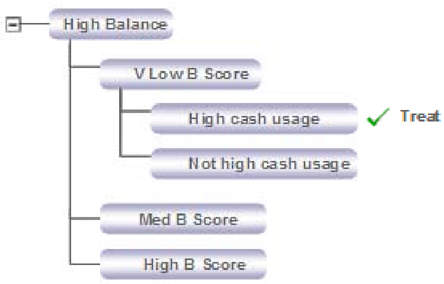
2.1 Pre-delinquent collections

Pre-delinquent collections is currently a relatively underused concept, where lenders proactively target and contact certain groups of accounts before they actually become delinquent. However, it has grown in popularity over the last 12 months in particular, as lenders attempt to stem the tide of mortgage and other credit losses by creating 'money management' teams that provide financial help and support to those customers most likely to default.

Both internal and external bureau triggers can be incorporated into pre-delinquency strategies to ensure a wider market picture of each customer is considered when determining default risk. Actions are then taken based on particular threshold levels being exceeded or predefined events occurring, even when the customer is still current with that particular lender.



Value: Pre-emptive collections give lenders the best opportunity to detect distressed accounts early. Lenders are then better positioned to compete successfully for payment ahead of other potential creditors and, in most cases, develop a promise to pay arrangement that has a high probability of success. Days sales outstanding and charge off levels will improve as a result of investing in pre-delinquency strategy development. Moreover, struggling customers are often grateful to have the chance to discuss payment options before their situation deteriorates and are likely to remain more loyal upon successful rehabilitation.

2.2 Past due but not delinquent

Collection of past due, but not delinquent, accounts uses a strategy designed to accurately treat certain groups of accounts before they actually become technically delinquent but after their payment due date. This anomaly sometimes occurs since many card processing systems do not actually register delinquency until the billing date, which can occur several days after the due date.

This strategy typically focuses on the highest risk groups only, ensuring they can be targeted for early and potentially stronger collections activity before normal collections activity would typically commence.

Value: Early identification and treatment of highest risk groups will reduce early stage collections balances and account volumes.

2.3 Automatic removal of additional lending and customer limits

In addition to accelerating treatment paths for higher risk delinquent or pre-delinquent accounts, many lenders also choose to reduce future risk by restricting further lending.

Strategies can be built, typically at mid delinquency stages but sometimes earlier, that use a combination of variables to trigger an action that will repress lending levels for that customer. This could be for a single account such as a credit card, or across several products and include revolving credit accounts. And, conversely, as the debt is paid down, a trigger can also be created to extend the credit available.

Value: The automation of limit suspension based on several predefined variables reduces the risk from further losses due to unconstrained credit access. In addition, profits will not be adversely impacted by the inaccurate throttling of credit access for high value, low risk customers.

2.4 Previous delinquency level

This is the concept of designing a collections strategy that takes the previous level of delinquency into account when determining what the next treatment action will be.

As multiple dunning levels can be incorporated, and multiple treatments defined per level, the resulting treatment paths can be large and fairly complex. However, it is the ability to implement unique, very tailored collection actions that makes this strategy so successful. For example, if an account was paying down from a previous higher level of delinquency, the treatment and communication could be very different, and much more supportive, than that for an account that had maintained the current level of delinquency.

Value: Whereas lenders have more control over accounts moving between delinquency levels and can tailor communication to make it more effective, customers too have a greater perceived sense of control with repayment efforts recognised. Habitual debtors also tend to be rehabilitated quicker, reducing DSO and roll rates.

2.5 Balance recoverable

The balance recoverable is a prediction of the amount that the delinquent customer will pay back over a defined period. It is useful in later stage delinquency to allocate resource to accounts most likely to pay the most back, while allowing harder to recover monies to be outsourced or sold to third party agents. Organisations can also establish a Net Present Value for each debt and may use this to determine appropriate pricing levels for debt sale.

Balance recoverable is calculated by multiplying the payment projection model/score by the current outstanding balance for an account, and can be used in combination with other variables to determine the next collections activity.

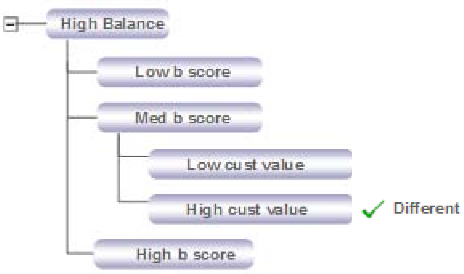
Value: Directing internal resources to the highest payback groups will improve the chance of recovery and reduce the cost of trying to collect from low probability groups. By factoring in variables that direct the account to the agent most likely to recover, the overall monies recovered will be improved.

2.6 Treatment by customer value

Few lenders can afford to upset profitable customers. Thus the ability to incorporate customer value into collections strategies is increasingly becoming a financial necessity.

Customer value variables are typically determined by the customer management system and are then passed to the collections system or decisioning engine to help define appropriate strategies and collections treatment paths.

Examples of high value accounts could be large savings or investments, or historic or predicted future revenue or profit growth.



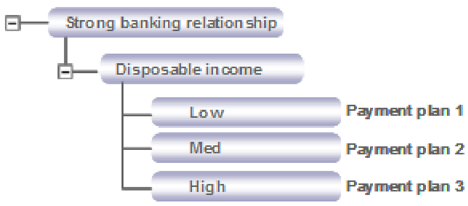
Value: A holistic collections strategy which attributes a value to the customer, not the account, will prevent unnecessary collections activity being taken on high value customers, saving on collections costs while minimising the risk of customer churn.

2.7 Pre-calculation of payment plans

The early identification of high risk customers will certainly give lenders an edge when it comes to securing payment or negotiating a payment plan, but unless the right plan is put in place the first time, few of them may remain current for very long.

Lenders need therefore to extract relevant, fresh, customer information and other internal affordability data and pre-calculate a promise to pay that drives the strongest net value for the lender, which is both acceptable and affordable to the customer

A strategy tree can then be created for pre-calculated optimal repayment plans, minimum payment plans and even settlement payment plans.



NB. Strong banking relationship – where a customer uses a current account with the bank via which their salary and typical daily income and expenditure activities are transacted.

Value: Data driven calculation of repayment plans will result in fewer broken promises, lower costs to collect, reduced charge offs and more rehabilitated customers.

2.8 Scripting driven from strategy segmentation

The rapidly growing number of delinquent accounts is forcing organisations to recruit new staff, cut down on training times and use third party resource much earlier in the collections cycle. But organisations cannot afford to let customer service standards slip nor collection inefficiencies and errors increase.

By defining a script for each customer segment at every node of the collections strategy, each collector conversation becomes much more tailored to the profile or unique situation of the customer.

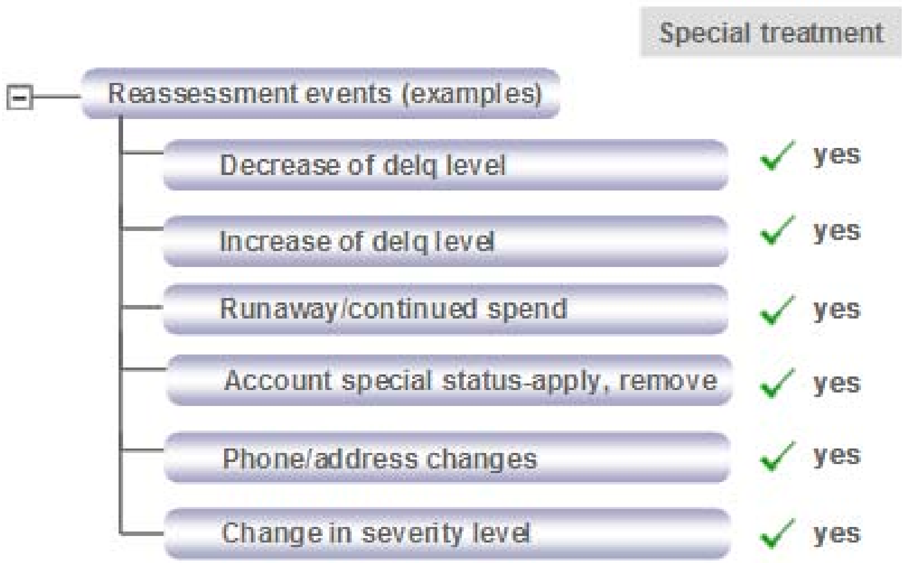
Value: Providing an accurate script for each operator for every type of collections call can cut down on errors, ensure consistency in approach and adherence to regulatory requirements. Collector efficiency will improve as will overall collections performance.

2.9 Dynamic reassessment

One of the most important aspects of a collections strategy is that it needs to stay current. Creditors need to react quickly to changes in personal or financial circumstance and adapt treatment paths accordingly.

Collection systems can be configured to update an account's status and implement immediate differentiated treatments on receipt of both internal and bureau based triggers.

Value: Dynamically reassessing each customer's status can assist in decreasing delinquency levels at all stages and lead to reduced charge offs. However, where the perceived risk decreases due to a customer's improved financial circumstance, lenders are then more likely to delay collections actions or to adopt a less aggressive tone. This saves on collections costs and can help improve the relationship, driving future revenue growth.



3. Summary

Many of the extended collections capabilities outlined in this guide are increasingly used throughout the financial sector. Proactive lenders are realising the value of drilling down deeper and using the full power of their decisioning or collections systems to deploy more effective collections strategies.

In the next guide, we explore a range of test and learn methodologies that lenders can use that will allow new scorecards, new strategies and new treatment paths to be created and trialled in real time with real data, with little adverse impact to ongoing collections activity.

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